

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA

PHOENIX, ARIZONA

FINANCIAL STATEMENTS

Year Ended June 30, 2005
with Report of Independent Auditors

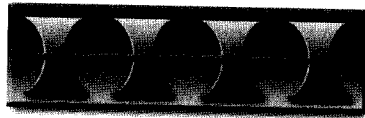
WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA

FINANCIAL STATEMENTS

Year Ended June 30, 2005

Table of Contents

Report of Independent Auditors	3 - 4
Management's Discussion and Analysis	5
Financial Statements:	
Statement of Net Assets	10
Statement of Revenues, Expenses, and Changes in Fund Net Assets	11
Statement of Cash Flows	12
Notes to Financial Statements	13
Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance With <i>Government Auditing Standards</i>	27



HENRY & HORNE, LLP
Advisors to Business

Independent Auditors' Report

Board of Directors
Water Infrastructure Finance Authority of Arizona
Phoenix, Arizona

We have audited the accompanying financial statements of the Water Infrastructure Finance Authority of Arizona, a discrete component unit of the State of Arizona, as of and for the year ended June 30, 2005, as listed in the table of contents. These financial statements are the responsibility of the Water Infrastructure Finance Authority of Arizona's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Water Infrastructure Finance Authority of Arizona, as of June 30, 2005, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 5 through 9 is not a required part of the financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

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CERTIFIED PUBLIC ACCOUNTANTS

In accordance with *Government Auditing Standards*, we have also issued our report dated October 4, 2005, on our consideration of Water Infrastructure Finance Authority of Arizona's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Henry. Hornz, LLP

October 4, 2005

Management's Discussion and Analysis

As management of the Water Infrastructure Finance Authority of Arizona (Authority), we offer readers of the Authority's financial statements this narrative overview and analysis of the financial activities of the Authority for the fiscal year ended June 30, 2005. We encourage readers to consider the information presented here in conjunction with the Authority's financial statements.

HIGHLIGHTS – BUSINESS TYPE ACTIVITIES

- In 2005, net assets increased by \$10 million and total assets decreased by \$1.7 million as compared to 2004.

USING THIS ANNUAL REPORT

The financial statements included in this annual report are those of a corporate and politic body of the State of Arizona. The following statements are included:

- Statement of net assets – reports the Authority's current financial resources, noncurrent financial resources, current obligations, long-term obligations, and the resulting net assets.
- Statement of revenues, expenses and changes in fund net assets – reports the Authority's program revenues, program expenses, nonprogram revenues, and capital contributions.
- Statement of cash flows – reports the Authority's cash flows from operating activities, investing, and non-capital activities.

STATEMENT OF NET ASSETS

Years Ended June 30,	2005	2004
Cash & Equivalents	\$147,746,319	\$232,328,770
Investments	68,081,810	68,081,810
Loans	489,071,853	409,169,550
All Other Assets	9,867,163	6,912,812
Total Assets	714,767,145	716,492,942
Bonds Payable	405,675,000	417,400,000
Interest Payable	5,027,882	5,105,470
All Other Liabilities	21,661,342	22,338,261
Total Liabilities	432,364,224	444,843,731
Net Assets Invested in Capital Assets	11,728	15,638
Restricted Capitalization for Grants	240,079,736	199,180,304
Unrestricted	42,311,457	72,453,269
Total Net Assets	\$282,402,921	\$271,649,211

The Authority net assets increased to \$282,402,921 during 2005, an increase of \$10,753,710 over 2004. The increase in net assets was primarily the result of capital contributions and loan activities.

REVIEW OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

The following table shows the condensed statement of revenues, expenses and changes in net assets for the past two years.

Years Ended June 30,	2005	2004
Program Revenues:		
Program loan interest revenue	\$9,287,547	\$5,240,954
Debt management fees	5,474,743	4,066,852
Total program revenue	14,762,290	9,307,806
Program Expenses:		
Administrative expenses	2,632,957	2,438,171
Technical/financial assistance	519,062	813,555
Program loan interest expense	17,884,713	12,876,283
Total program expenses	21,036,732	16,128,009
Program loss	(6,274,442)	(6,820,203)
Non-program revenues	9,551,368	6,663,320
Income before contributions	3,276,926	(156,883)
Capital contributions	7,476,784	33,422,648
Change in net assets	10,753,710	33,265,765
Beginning net assets	271,649,211	238,383,446
Ending net assets	\$282,402,921	\$271,649,211

**Restated in 2004 due to prior period adjustment of (\$283,722).

Compared to 2004, total expenses increased by \$4.9 million. The increase was primarily due to expenses associated with the Authority's bonds.

WIFA relied on significant federal capital contributions and bond proceeds to fund loans in 2005 and drew contributions from multiple open federal capitalization grants.

BUDGETARY HIGHLIGHTS

The Authority's Board of Directors adopted an operating budget of \$1,712,685 for the period July 1, 2004 through June 30, 2005.

<u>Budget Line Item</u>	<u>Amount</u>
Salaries & Benefits	\$1,159,335
Professional & Outside Services	211,550
In State Travel	19,400
Out of State Travel	22,000
Other Operating	244,300
Equipment	13,600
Indirect Cost	42,500
Total	<u><u>\$1,712,685</u></u>

CAPITAL ASSETS

The Authority's capital assets consist of computer equipment. In 2004, the Authority purchased \$13,459 of computer equipment. There were no new purchases of capital assets in 2005.

DEBT OUTSTANDING

Years Ended June 30,	<u>2005</u>	<u>2004</u>
Beginning balance	\$ 417,400,000	\$ 230,280,000
Refunded Bonds	-	(95,445,000)
Refunding Bonds	-	97,100,000
Additions	-	195,980,00
Payments	(11,725,000)	(10,515,000)
Ending balance	<u><u>\$ 405,675,000</u></u>	<u><u>\$ 417,400,000</u></u>

ECONOMIC AND OTHER FACTORS

Drinking Water Standard for Arsenic

In October 2001, the United States Environmental Protection Agency adopted a new standard for the amount of arsenic permissible within drinking water. The new standard decreased the maximum amount of arsenic from 50 parts per billion to 10 parts per billion. According to estimates from the Arizona Department of Environmental Quality, the new arsenic standard will affect

approximately 3,000,000 customers of drinking water systems throughout Arizona. Under the current requirements, drinking water systems have until January 23, 2006 to achieve compliance with the new standard or will fall out of compliance and face penalties.

As a result of the need to comply with the new federal standard, the Authority anticipates continued high demand for its drinking water financial assistance from small water systems. Many of these small water systems will require significant rate increases to accommodate the capital and operating costs associated with arsenic treatment. Accordingly, the Authority anticipates providing increased financial assistance in 2006.

Authority Automation Efforts

The Authority continues to develop and implement fiscal related applications to automate its financial activity.

Inequity in the Clean Water State Revolving Fund (CWSRF) Capitalization Grant Funding Allocation

Congress appropriates funding to EPA which, in turn, grants allocations to states to capitalize CWSRFs in accordance with state-by-state federally enacted allocation percentages. As originally intended by Congress, CWSRF allocations to states should be based on population and documented needs.

The present allocation percentages are based on a 1977 formula using data from the 1970 census and the 1974 wastewater needs survey. Present allocations favor the Northeast and Midwest regions at the expense of the remainder of the country, particularly the Southeast and Southwest regions. While the population of the U.S. continues to migrate south and west, the vast majority of the funding for infrastructure remains in the Northeast and Midwest.

Based on Census Bureau data, Arizona's 2000 population approximates 5.1 million, ranking 20th for population by state. However, Arizona is 53rd out of 53 for CWSRF allocations per capita.

Based on EPA's 2002 Needs Survey, Arizona certified nearly \$6.3 billion in wastewater infrastructure needs, ranking 10th for needs by state. However, Arizona is 52 out of 52 for CWSRF Allocations compared to certified need.

A new clean water needs survey was completed in Fy 05 with the results expected in Fy 06.

Arizona currently receives only 0.68% of the CWSRF appropriation. Based on allocations to states with similar needs, Arizona should receive 3.54% of the CWSRF appropriation, more than five times more than it currently receives.

A conservative estimate indicates that Arizona has lost over \$216 million in allocations since 1989. In effect, Arizona's taxpayers subsidize infrastructure in

other states and pay more for the same infrastructure within Arizona as the result of the funding disparity.

FINANCIAL CONTACT

The Authority's financial statements present users with a general overview of the Authority's finances and demonstrate the Authority's accountability. If you have any questions about the report or require additional financial information, please contact Mona Spellman, Controller, Water Infrastructure Finance Authority of Arizona, 1110 West Washington, Suite 290, Phoenix, Arizona 85007 or by phone at (602) 364-1310 or toll-free at (877) 298-0425.

Water Infrastructure Finance Authority of Arizona
Statement of Net Assets
Proprietary Funds
June 30, 2005

	Business-type Activities-Enterprise Funds			
	Clean Water Revolving Fund	Drinking Water Revolving Fund	Hardship Grant Fund	Total
ASSETS				
Current assets:				
Cash and cash equivalents:				
Cash with treasurer	\$ 68,377,743	\$ 63,226,426	\$ 15,962	\$ 131,620,131
Cash with trustee	11,190,554	4,935,634	-	16,126,188
Total cash and cash equivalents	79,568,297	68,162,060	15,962	147,746,319
Receivables, net of uncollectibles				
Debt management	1,357,118	752,687	-	2,109,805
Interest	3,868,097	1,471,365	-	5,339,462
Due (to) from other funds	2,208,453	(2,276,653)	68,200	-
Total current assets	87,001,965	68,109,459	84,162	155,195,586
Noncurrent assets:				
Investments	56,692,519	11,389,291	-	68,081,810
Program loans	349,093,744	139,978,109	-	489,071,853
Deferred bond costs	1,728,794	677,374	-	2,406,168
Capital assets (net of depreciation)	5,864	5,864	-	11,728
Total noncurrent assets	407,520,921	152,050,638	-	559,571,559
Total assets	494,522,886	220,160,097	84,162	714,767,145
LIABILITIES				
Current liabilities:				
Accrued payroll	7,831	7,831	-	15,662
Compensated absences	13,007	13,007	-	26,014
Interest payable	3,626,538	1,401,344	-	5,027,882
Bonds payable-current	20,390,323	8,124,677	-	28,515,000
Total current liabilities	24,037,699	9,546,859	-	33,584,558
Noncurrent liabilities:				
Loan reserve	214,583	1,807,520	-	2,022,103
Unamortized bond premiums	18,032,885	10,173,204	-	28,206,089
Deferred amount on retirement of bonds	(5,667,012)	(2,941,514)	-	(8,608,526)
Bonds payable	262,106,630	115,053,370	-	377,160,000
Total noncurrent liabilities	274,687,086	124,092,580	-	398,779,666
Total liabilities	298,724,785	133,639,439	-	432,364,224
NET ASSETS				
Net assets invested in capital assets	5,864	5,864	-	11,728
Restricted for capitalization grants	163,710,285	76,369,451	-	240,079,736
Unrestricted	32,081,952	10,145,343	84,162	42,311,457
Total net assets	\$ 195,798,101	\$ 86,520,658	\$ 84,162	\$ 282,402,921

See accompanying notes.

Water Infrastructure Finance Authority of Arizona
Statement of Revenues, Expenses and Changes in Fund Net Assets
Proprietary Funds
For The Year Ended June 30, 2005

	Business-type Activities-Enterprise Funds			
	Clean Water Revolving Fund	Drinking Water Revolving Fund	Hardship Grant Fund	Total
Program revenues:				
Program loan interest revenue	\$ 6,507,810	\$ 2,779,737	\$ -	\$ 9,287,547
Debt management fees	3,313,063	2,161,680	-	5,474,743
Total program revenues	<u>9,820,873</u>	<u>4,941,417</u>	<u>-</u>	<u>14,762,290</u>
Program expenses:				
Administrative expenses	791,653	1,657,020	-	2,448,673
Depreciation	1,955	1,955	-	3,910
Technical assistance	330,815	188,247	-	519,062
Financial assistance	180,374	-	-	180,374
Program loan interest expense	12,766,311	5,118,402	-	17,884,713
Hardship grant expense	-	-	-	-
Total program expenses	<u>14,071,108</u>	<u>6,965,624</u>	<u>-</u>	<u>21,036,732</u>
Program loss	<u>(4,250,235)</u>	<u>(2,024,207)</u>	<u>-</u>	<u>(6,274,442)</u>
Nonprogram revenues:				
Administrative grants	102,879	868,583	-	971,462
Investment earnings	5,983,971	2,595,935	-	8,579,906
Total nonprogram revenues	<u>6,086,850</u>	<u>3,464,518</u>	<u>-</u>	<u>9,551,368</u>
Income before contributions and transfers	1,836,615	1,440,311	-	3,276,926
Capital contributions-federal	75,000	4,956,684	-	5,031,684
Capital contributions-state	893,200	1,551,900	-	2,445,100
Transfers in (out)	151	(151)	-	-
Change in net assets	<u>2,804,966</u>	<u>7,948,744</u>	<u>-</u>	<u>10,753,710</u>
Total net assets-beginning of year	192,993,135	78,571,914	84,162	271,649,211
Total net assets-end of year	<u>\$ 195,798,101</u>	<u>\$ 86,520,658</u>	<u>\$ 84,162</u>	<u>\$ 282,402,921</u>

See accompanying notes.

Water Infrastructure Finance Authority of Arizona
Statement of Cash Flows
Proprietary Funds
For The Year Ended June 30, 2005

CASH FLOWS FROM OPERATING ACTIVITIES	Business-type Activities-Enterprise Funds			Total
	Clean Water Revolving Fund	Drinking Water Revolving Fund	Hardship Grant Fund	
Receipt of program loans	\$ 22,306,366	\$ 5,739,373	\$ -	\$ 28,045,739
Loans made to borrowers	(73,572,336)	(26,870,741)	-	(100,443,077)
Receipt of debt management fees	2,303,709	1,941,560	-	4,245,269
Receipt of loan reserves	35,710	418,198	-	453,908
Payment of administrative costs	(807,369)	(1,672,736)	-	(2,480,105)
Payment of technical assistance costs	(330,815)	(188,247)	-	(519,062)
Payment of financial assistance costs	(180,374)	-	-	(180,374)
Payment of program loan costs	(13,377,943)	(5,510,494)	-	(18,888,437)
Net cash used by operating activities	(63,623,052)	(26,143,087)	-	(89,766,139)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
Receipt (payment) of interfund	213,361	(213,361)	-	-
Principal paid on bonds	(9,250,800)	(2,474,200)	-	(11,725,000)
Receipt of administrative grants	102,879	868,583	-	971,462
Capital contributions	968,200	6,508,584	-	7,476,784
Net cash provided (used) by noncapital financing activities	(7,966,360)	4,689,606	-	(3,276,754)
CASH FLOWS FROM INVESTING ACTIVITIES				
Interest received on investments	5,900,738	2,559,704	-	8,460,442
Net cash provided by investing activities	5,900,738	2,559,704	-	8,460,442
Net decrease in cash and cash equivalents	(65,688,674)	(18,893,777)	-	(84,582,451)
Cash and cash equivalents at beginning of year	145,256,971	87,055,837	15,962	232,328,770
Cash and cash equivalents at end of year	\$ 79,568,297	\$ 68,162,060	\$ 15,962	\$ 147,746,319

See accompanying notes.

Water Infrastructure Finance Authority of Arizona
Statement of Cash Flows
Proprietary Funds
For The Year Ended June 30, 2005

	Business-type Activities-Enterprise Funds			
	Clean Water Revolving Fund	Drinking Water Revolving Fund	Hardship Grant Fund	Total
Reconciliation of program loss to net cash used by operating activities:				
Program loss	\$ (4,250,235)	\$ (2,024,207)	\$ -	\$ (6,274,442)
Adjustments to reconcile program loss to net cash used by operating activities:				
Depreciation	1,955	1,955		3,910
Amortization of bond related costs	(524,456)	(401,680)	-	(926,136)
(Increase) decrease in:				
Program loans	(56,618,994)	(23,283,309)	-	(79,902,303)
Debt management receivable	(1,009,354)	(220,120)	-	(1,229,474)
Interest receivable	(1,154,786)	(627,796)	-	(1,782,582)
Increase (decrease) in:				
Accrued payroll	(2,324)	(2,324)	-	(4,648)
Compensated absences	(13,392)	(13,392)	-	(26,784)
Interest payable	(87,176)	9,588	-	(77,588)
Loan reserve	35,710	418,198	-	453,908
Total adjustments	(59,372,817)	(24,118,880)	-	(83,491,697)
Net cash used by operating activities	<u>\$ (63,623,052)</u>	<u>\$ (26,143,087)</u>	<u>\$ -</u>	<u>\$ (89,766,139)</u>

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The Water Infrastructure Finance Authority of Arizona (WIFA) is a political body and a component unit of the State of Arizona (State). WIFA's financial information is discretely presented in the Comprehensive Annual Financial Report of the State of Arizona. It is authorized to administer the Clean Water Revolving Fund and The Drinking Water Revolving Fund (Fund). WIFA is governed by a twelve-member board of directors. The day-to-day administrative functions of WIFA are overseen by WIFA's Executive Director and other staff employed by WIFA.

The Clean Water Revolving Fund was created pursuant to the Federal Water Pollution Control Act of 1972, as amended by the Water Quality Act of 1987 (Clean Water Act), which required the State of Arizona to establish the Fund to accept federal capitalization grants for publicly owned wastewater treatment projects. The purpose of the fund is to provide financial assistance, including loans to political subdivisions and Indian tribes to finance construction, acquisition, restoration or rebuilding of wastewater treatment facilities.

WIFA has an agreement with the Environmental Protection Agency to administer the Drinking Water Revolving Fund pursuant to the Safe Drinking Water Act. The fund was established to provide water facility loans including forgivable principal to political subdivisions of this state, Indian Tribes and other eligible entities as determined by the board pursuant to the Safe Drinking Water Act, make drinking water facility loans, purchase or refinance debt obligations of drinking water facilities, assist in purchasing insurance for local drinking water facility bond obligations, pay the costs to administer the fund, fund other programs pursuant to the Safe Drinking Water Act and provide linked deposit guarantees through third party lenders with recourse against deposit if payments are not made when due.

The Funds are authorized to be capitalized through (i) moneys, if any, appropriated by the State Legislature, (ii) federal capitalization grants and other federal moneys received by WIFA to fund the Fund, (iii) proceeds of WIFA's bonds, including bonds issued to provide matching State moneys as required by the Clean Water Act, (iv) moneys received from political subdivisions or Indian tribes as repayment of loans from the Fund, including interest and penalties thereon, (v) interest and other income received from investing moneys of the Fund, and (vi) gifts, grants and donations received from any public or private source. In order to receive federal capitalization grants, the State must provide matching funds in a ratio of \$1 of State matching funds for every \$5 of federal capitalization grants. The State began appropriating money for deposit into the Funds in 1998. Previously the State matching funds were provided from proceeds of the WIFA's capitalization bonds.

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Reporting Entity (Continued)

The accompanying financial statements present the Clean Water Revolving Fund, Drinking Water Revolving Fund and the Hardship Grant Fund, which includes all of the revenues and the administrative expenses of WIFA.

Fund Type

WIFA plans to maintain the federal capitalization grants as the fund's restricted net assets. Therefore, the periodic determination of revenues earned, expenses incurred, and changes in net assets are appropriate for capital maintenance, public policy, management control, accountability and other purposes. As a result, the accounting records are maintained as an enterprise fund. Only earnings from the administrative grants, debt management fees and interest earned on accumulated excess administrative income can be expended for expenses or utilized to match federal grants.

WIFA distinguishes program revenues and expenses from non-program items. Program revenues and expenses generally result from providing services in connection with financing and administering moneys for the Clean and Drinking Water Revolving Funds. The principal program revenues of WIFA are program loan interest and management fees. WIFA's program expenses are administrative, program loan costs and grant related expenses. All revenues and expenses not meeting this definition are reported as non-program revenues and expenses.

Measurement Focus and Basis of Accounting

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. WIFA's financial statements are reported using the economic resources measurement focus. WIFA's accounting records are maintained on the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when they are earned and expenses are recognized when they are incurred. Pursuant to GASB Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting, the WIFA follows GASB guidance as applicable to proprietary funds, and Financial Accounting Standards Boards Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins issued on or before November 30, 1989 that do not conflict with or contradict GASB Pronouncements.

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investments

WIFA has adopted provisions of Statement No. 31 of the Governmental Accounting Standards Board (GASB), Accounting and Financial Reporting for Certain Investments and for External Investment Pools. This standard requires certain investments to be reported at fair value rather than at cost.

Investments in Guaranteed Investment Contracts are stated at cost, since they are non-participating contracts. The investment of excess revenue in the 2001 Master Trust Indenture is stated at fair value, which approximates cost.

Cash Equivalents

WIFA considers all highly liquid debt instruments purchased with maturities of three months or less at acquisition date to be cash equivalents. Cash equivalents are stated at cost, which approximates market.

Capital Assets

Capital assets acquired by the Funds are stated at cost. The capitalization threshold has been set at \$5,000. Depreciation has been allocated using the straight-line method over the following estimated useful lives:

Computer and Peripheral Equipment	3 - 5 years
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Compensated Absences

WIFA employees accrue vested annual leave at a variable rate based on years of service. Employees forfeit accumulated annual leave in excess of 320 hours at the end of a calendar year. Any employee who separates from WIFA service is paid for all unused and unforfeited annual leave at the employee's rate of pay at the time of separation.

Sick leave includes any approved period of paid absence granted an employee due to illness, injury or disability. Employees accrue sick leave at the rate of eight hours per month without an accumulation limit. Because sick leave benefits do not vest with employees, a liability for sick leave is not accrued in the financial statements.

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Long-term Obligations

Long-term debt is reported as fund liabilities in the applicable fund's statement of net assets. Bond premiums, bond issuance costs and loss on retirement of bonds are deferred and amortized over the life of the bonds using the straight-line method.

Net Assets

WIFA restricts amounts received from the federal and state government for the purpose of providing financial assistance for publicly owned wastewater treatment and water facilities.

Grants

Grants restricted for program loans are recorded as contributions. Grants that are used for operating purposes are recorded as revenue. Federal grants for project related expenses might not be drawn until qualifying expenditures are incurred.

Fund Administration

Employees of WIFA perform administration of the Funds. Expenses relating to the administration are funded from the capital facility grant (up to a maximum of 4 percent of the capital facility grant) and fees charged to loan recipients (see Note 8).

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

NOTE 2 CASH AND INVESTMENTS

Cash Deposits

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, an entity will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party.

At June 30, 2005, the carrying amount of WIFA's cash with treasurer totaled \$131,620,131 of which \$126,332,192 was invested in the State Agency's pool number 3. A copy of the audited financial statements may be obtained by contacting the Office of the State Treasurer.

At June 30, 2005, the carrying amount of WIFA's cash with trustee totaled \$16,126,188. WIFA maintains their cash held by trustee in an irrevocable trust account in the name of WIFA held by the trust department of a financial institution located in Phoenix, Arizona (separate from all other funds and investments of the trustee). These balances are directed by the State Treasurer to be invested in a full faith and credit money market fund that is not insured by the Federal Deposit Insurance Corporation or collateralized by the trustee.

Investments

The State Treasurer directs WIFA's investments. ARS 35-312 and ARS 35-313 require the State Treasurer to invest in obligations of the U.S. or its agencies including sponsored agencies, corporations, sponsored corporations or instrumentalities, collateralized repurchase agreements, bonds or other evidence of indebtedness of the State of Arizona or its political subdivisions, commercial paper, bankers acceptances, certificates of deposit, interest-bearing savings accounts and bonds, debentures, notes and other evidences of indebtedness issued by U.S. corporations meeting certain rating criteria. WIFA's investments at June 30, 2005, consisted of collateralized guaranteed investment contracts issued by domestic banks, a monoline insurer and insurance company, and a foreign bank acting through its New York branch. The guaranteed investment contracts are not insured by the Federal Deposit Insurance Corporation.

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. Information about the sensitivity of the fair values of WIFA's investments to market interest rate fluctuations is provided by the following table that shows the distribution of WIFA's investments by maturity:

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

NOTE 2 CASH AND INVESTMENTS (Continued)

Investment Type		Remaining Maturity (In Months)			
		12 Months or Less	13 to 24 Months	25 to 60 Months	More Than 60 Months
State Investment Pool	\$ 126,332,192	\$ 126,332,192	\$ -	\$ -	\$ -
Money Market Funds	16,126,188	16,126,188	-	-	-
Guaranteed Investment Contracts	68,081,810	-	-	11,467,864	56,613,946
	<u>\$ 210,540,190</u>	<u>\$ 142,458,380</u>	<u>\$ -</u>	<u>\$ 11,467,864</u>	<u>\$ 56,613,946</u>

Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Presented below is the Standard & Poor's rating as of year-end for each investment type.

Investment Type		Ratings as of Year-End			
		AAA	AA	A	Unrated
State Investment Pool	\$ 126,332,192	\$ -	\$ -	\$ -	\$ 126,332,192
Money Market Funds	16,126,188	-	-	-	16,126,188
Guaranteed Investment Contracts	68,081,810	68,081,810	-	-	-
	<u>\$ 210,540,190</u>	<u>\$ 68,081,810</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 142,458,380</u>

If any of the bank's credit rating falls below levels defined in the investment contracts, the State Treasurer may direct the bank to enter into a repurchase agreement with the Trustee pursuant to which the bank shall sell and deliver to the Trustee certain U.S. government obligations in a principal amount equal to invested moneys and accrued interest. If the rating falls below "A" the Trustee shall have the right to withdraw all amounts invested and accrued interest.

Concentration of Credit Risk

The investment policy of WIFA contains no limitations on the amount that can be invested in any one issuer. Investments in any one issuer are as follows:

Issuer	Investment Type	Reported Amount
State Investment Pool	State Investment Pool	\$ 126,332,192
First American Prime Obligations Fund	Money Market	16,126,188
Bayerische Landesbank	Guaranteed Investment Contract	40,585,505
Morgan Guarantee Trust Company of New York	Guaranteed Investment Contract	2,343,794
AIG Matched Funding Corp.	Guaranteed Investment Contract	25,152,511
		<u>\$ 210,540,190</u>

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

NOTE 3 PROGRAM LOANS

The Funds have made loans to local governments and others in Arizona to finance various projects pursuant to the requirements of the Clean Water and Safe Drinking Water Acts. The loans are generally payable in semiannual installments due January 1 and July 1 of each year, including interest. However, several loans are payable monthly or quarterly. Changes in the program loans are as follows:

	July 1, 2004	Increases	Decreases	June 30, 2005
Clean Water Fund	\$292,474,750	\$ 73,572,336	\$(16,953,342)	\$349,093,744
Drinking Water Fund	116,694,800	26,870,741	(3,587,432)	139,978,109
	<u>\$409,169,550</u>	<u>\$100,443,077</u>	<u>\$(20,540,774)</u>	<u>\$489,071,853</u>

Repayment of these loans will be made from pledged property taxes, net revenues from the systems, transaction privilege taxes or from special assessments. Most loans have a .3 to 4.0 percent annual administrative fee.

Some program loans require a monthly or quarterly payment into a debt service reserve to assure payments of the loans. The debt service reserve is a liability of WIFA to the borrowers and interest on the reserve accrues to the borrowers.

NOTE 4 CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2005 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
<u>Clean Water Fund</u>				
Computers & Peripheral Equipment	\$ 50,734	\$ -	\$ -	\$ 50,734
Less Accumulated Depreciation	(42,915)	(1,955)	-	(44,869)
Clean Water Capital Assets, net	<u>7,819</u>	<u>(1,955)</u>	<u>-</u>	<u>5,864</u>
<u>Drinking Water Fund</u>				
Computers & Peripheral Equipment	50,734	-	-	50,734
Less Accumulated Depreciation	(42,915)	(1,955)	-	(44,869)
Drinking Water Capital Assets, net	<u>7,819</u>	<u>(1,955)</u>	<u>-</u>	<u>5,864</u>
<u>Clean and Drinking Water Funds</u>				
Computers & Peripheral Equipment	101,468	-	-	101,468
Less Accumulated Depreciation	(85,830)	(3,910)	-	(89,738)
Clean and Drinking Water Capital Assets, net	<u>\$ 15,638</u>	<u>\$ (3,910)</u>	<u>\$ -</u>	<u>\$ 11,728</u>

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

NOTE 5 COMPENSATED ABSENCES

The compensated absences activity for June 30, 2005 was as follows:

Compensated Absences for:	July 1, 2004	Additions	Reductions	June 30, 2005	Estimated Current Portion
Clean Water	\$ 26,399	\$ 10,019	\$ 3,411	\$ 13,007	\$ 13,007
Drinking Water	26,399	10,019	23,411	13,007	13,007
Total	<u>\$ 52,798</u>	<u>\$ 20,038</u>	<u>\$ 46,822</u>	<u>\$ 26,014</u>	<u>\$ 26,014</u>

NOTE 6 RETIREMENT AND PENSION PLAN

Arizona State Retirement Plan

Plan Description. The Arizona State Retirement System (ASRS) administers a cost sharing multiple-employer defined benefit pension plan that covers employees of WIFA. The ASRS is governed by the Arizona State Retirement System Board according to the provisions of A.R.S. Title 38, Chapter 5, Article 2. Benefits are established by state statute and generally provide retirement, death, long-term disability, survivor, and health insurance premium benefits. ASRS issues a publicly available report that includes financial statements and required supplementary information. The report may be obtained in writing at ASRS, 3300 N. Central Avenue, P.O. Box 33910, Phoenix, Arizona 85067-3910 or by calling 602-240-2200 or 1-800-621-3778.

Funding Policy. The Arizona State Legislature has the authority to establish and amend benefits provisions and contributions for active plan members. For the years ended June 30, 2005, 2004 and 2003, active ASRS members and WIFA were each required by statute to contribute at the actuarially determined rate of 5.20, 5.20 and 2.49 percent (rate includes .50 percent long-term disability for 2005 and 2004 and .49 percent for 2003), respectively, of the members' annual covered payroll. WIFA's contributions to ASRS for the years ended June 30, 2005, 2004 and 2003 were \$39,604, \$39,431 and \$14,209, respectively.

NOTE 7 BONDS PAYABLE

Bonds payable at June 30, 2005 are summarized below. The bonds are callable and interest is payable semiannually. The bonds are special obligations of WIFA payable solely from and secured by the Fund's assets. The obligations are not obligations, general, specific or otherwise, of the State of Arizona or any other political subdivision thereof other than WIFA.

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

NOTE 7 BONDS PAYABLE (Continued)

\$3,270,000 Financial Assistance Revenue Bonds, Series 1995, due in annual principal installments ranging from \$225,000 to \$410,000, plus semiannual interest ranging from 4.40% to 5.50% through July 1, 2009.	\$1,935,000
\$585,000 Capitalization Revenue Bonds, Series 1995, due in annual principal installments ranging from \$80,000 to \$125,000, plus semiannual interest ranging from 4.40% to 5.00% through July 1, 2005.	125,000
\$9,730,000 Financial Assistance Revenue Bonds, Series 1996A, due in annual principal installments ranging from \$360,000 to \$1,870,000, plus semiannual interest ranging from 3.70% to 5.50% through July 1, 2012.	9,370,000
\$1,135,000 Capitalization Revenue Bonds, Series 1996A, due in annual principal installments ranging from \$140,000 to \$385,000, plus semiannual interest ranging from 3.70% to 5.00% through July 1, 2005.	220,000
\$20,125,000 Financial Assistance Revenue Bonds, Series 1997A, due in annual principal installments ranging from \$845,000 to \$1,415,000, plus semiannual interest ranging from 4.20% to 6.1% through July 1, 2008.	5,035,000
\$3,330,000 Capitalization Revenue Bonds, Series 1997A, due in annual principal installments ranging from \$335,000 to \$625,000, plus semiannual interest ranging from 4.20% to 4.65% through July 1, 2005.	625,000
\$35,370,000 Financial Assistance Revenue Bonds, Series 1998A, due in annual principal installments ranging from \$1,985,000 to \$2,190,000, beginning July 1, 1999, plus semiannual interest ranging from 3.8% to 5% through July 1, 2008.	7,875,000
\$64,000,000 Water Quality Revenue Refunding Bonds, Series 1999, due in annual principal installments ranging from \$2,330,000 to \$8,190,000, plus semiannual interest ranging from 4.0% to 5.625% through October 1, 2017.	54,255,000
\$110,000,000 Water Quality Revenue Bonds, Series 2001A, due in annual principal installments ranging from \$3,780,000 to \$8,075,000, plus semiannual interest ranging from 4.0% to 5.375% through October 1, 2011.	33,280,000

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

NOTE 7 BONDS PAYABLE (Continued)

\$97,100,000 Water Quality Revenue Refunding Bonds, Series 2004, due in annual principal installments ranging from \$125,000 to \$4,825,000, plus semi annual interest ranging from 2.0% to 5.0% through October 1, 2021. \$ 96,975,000

\$195,980,000 Water Quality Revenue Bonds, Series 2004, due in annual principal installments ranging from \$5,500,000 to \$15,080,000, plus semi annual interest ranging from 2.0% to 5.0% through October 1, 2024. 195,980,000
\$ 405,675,000

A summary of changes in bonds payable is set forth below:

	<u>July 1, 2004</u>	<u>Issued</u>	<u>Retired</u>	<u>June 30, 2005</u>
Financial Assistance Revenue				
Bonds Series 1992 A	\$ 315,000	\$ -	\$ 315,000	\$ -
Capitalization Revenue Bonds				
Series 1992 A	90,000	-	90,000	-
Financial Assistance Revenue				
Bonds Series 1995	2,160,000	-	225,000	1,935,000
Capitalization Revenue Bonds				
Series 1995	260,000	-	155,000	125,000
Financial Assistance Revenue				
Bonds Series 1996A	9,730,000	-	360,000	9,370,000
Capitalization Revenue Bonds				
Series 1996A	605,000	-	385,000	220,000
Financial Assistance Revenue				
Bonds Series 1997A	5,985,000	-	950,000	5,035,000
Capitalization Revenue Bonds				
Series 1997A	960,000	-	335,000	625,000
Financial Assistance Revenue				
Bonds Series 1998A	9,815,000	-	1,940,000	7,875,000
Water Quality Refunding				
Bonds Series 1999	56,935,000	-	2,680,000	54,255,000
Water Quality Revenue				
Bonds Series 2001A	37,445,000	-	4,165,000	33,280,000
Water Quality Revenue				
Bonds Series 2004A	195,980,000	-	-	195,980,000
Water Quality Refunding				
Bonds Series 2004A	<u>97,100,000</u>	<u>-</u>	<u>125,000</u>	<u>96,975,000</u>
	<u>\$ 417,400,000</u>	<u>\$ -</u>	<u>\$ 11,725,000</u>	<u>\$ 405,675,000</u>

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

NOTE 7 BONDS PAYABLE (Continued)

Bonds by Fund are as follows:

Arizona Clean Water Revolving Fund	\$ 282,496,953
Arizona Drinking Water Revolving Fund	123,178,047
	<u>\$ 405,675,000</u>

The Clean Water Fund's bond debt service requirements to maturity, including interest, are as follows:

Year Ending June 30,	Clean Water		
	Principal	Interest	Total
2006	\$ 20,390,323	\$ 12,953,630	\$ 33,343,953
2007	18,407,793	12,256,573	30,664,366
2008	16,678,405	11,530,538	28,208,943
2009	17,240,555	10,769,878	28,010,433
2010	15,143,250	10,036,582	25,179,832
2011-2015	83,485,606	37,609,131	121,094,737
2016-2020	69,612,306	18,092,789	87,705,095
2021-2025	41,538,715	3,759,012	45,297,727
Total Long-Term Debt	282,496,953	117,008,133	399,505,086
Less Current Portion	(20,390,323)	(12,953,630)	(33,343,953)
Noncurrent Portion	<u>\$ 262,106,630</u>	<u>\$104,054,503</u>	<u>\$ 366,161,133</u>

The Drinking Water Fund's bond debt service requirements to maturity, including interest, are as follows:

Year Ending June 30,	Drinking Water		
	Principal	Interest	Total
2006	\$ 8,124,677	\$ 5,415,662	\$ 13,540,339
2007	6,702,206	5,192,952	11,895,158
2008	6,346,595	4,951,127	11,297,722
2009	6,429,445	4,674,560	11,104,005
2010	6,976,750	4,379,879	11,356,629
2011-2015	33,219,394	17,051,450	50,270,844
2016-2020	31,242,693	9,419,883	40,662,576
2021-2025	24,136,287	2,068,050	26,204,337
Total Long-Term Debt	123,178,047	53,153,563	176,331,610
Less Current Portion	(8,124,677)	(5,415,662)	(13,540,339)
Noncurrent Portion	<u>\$ 115,053,370</u>	<u>\$ 47,737,901</u>	<u>\$ 162,791,271</u>

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

NOTE 7 BONDS PAYABLE (Continued)

WIFA's total bond debt service requirements to maturity, including interest, are as follows:

Year Ending June 30,	Total Clean and Drinking Water		
	Principal	Interest	Total
2006	\$ 28,515,000	\$ 18,369,292	\$ 46,884,292
2007	25,109,999	17,449,525	42,559,524
2008	23,025,000	16,481,665	39,506,665
2009	23,670,000	15,444,438	39,114,438
2010	22,120,000	14,416,461	36,536,461
2011-2015	116,705,000	54,660,581	171,365,581
2016-2020	100,854,999	27,512,672	128,367,671
2021-2025	65,675,002	5,827,062	71,502,064
Total Long-Term Debt	405,675,000	170,161,696	575,836,696
Less Current Portion	(28,515,000)	(18,369,292)	(46,884,292)
Noncurrent Portion	\$ 377,160,000	\$ 151,792,404	\$ 528,952,404

On September 8, 1999, WIFA issued \$64,000,000 of Water Quality Refunding Bonds to do an advance refunding of the 1991A bonds and part of the 1992A, 1995A and 1996A bonds. Under the terms of the refunding issue, sufficient assets to pay all principal and interest on the refunded bond issues have been placed in irrevocable trust accounts at commercial banks and invested in U.S. Government Securities which, together with interest earned thereon, will provide amounts sufficient for future payment of principal and interest of the issues refunded. The amount outstanding on those bonds as of June 30, 2005 is \$17,275,000. These bonds have been fully defeased.

The net present value cash flow for savings on issuing the refunding bonds at a 5.271% bond yield was \$237,387.

On April 7, 2004, WIFA issued \$97,100,000 of Water Quality Refunding Bonds to do an advance refunding part of the 1992, 1997A, 1998A and 2001 bonds. Under the terms of the refunding issue, sufficient assets to pay all principal and interest on the refunded bond issues have been placed in irrevocable trust accounts at commercial banks and invested in U.S. Government Securities which, together with interest earned thereon, will provide amounts sufficient for future payment of principal and interest of the issues refunded. The amount outstanding on those bonds as of June 30, 2005 is \$91,215,000. These bonds have been fully defeased.

The net present value cash flow for savings on issuing the refunding bonds at a 3.213% bond yield was \$3,120,247.

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

NOTE 7 BONDS PAYABLE (Continued)

The \$8,608,526 deferred amount on retirement of bonds is being amortized over the lives of the defeased bonds on the straight-line basis. Annual amortization is \$408,707 and \$173,030 for Clean Water Revolving and Drinking Water Revolving Funds, respectively. Amortization has been offset against interest expense.

NOTE 8 ADMINISTRATIVE REVENUES AND EXPENSES

WIFA is authorized to utilize a portion of the facility grant as an administrative grant (not to exceed 4% of the net capital facility grant). These funds are deposited to an administrative grant account maintained by WIFA which is accounted for in a separate fund at the treasurer's office.

WIFA also receives a loan origination fee on most loans and servicing fees assessed on the outstanding loan balance from each of the local borrowers (Debt Management Revenue). These fees are used to defray program administration expenses, and are collected and recorded by WIFA as separate funds at the treasurer's office.

The administrative expenses reported by WIFA for the year ended June 30, 2005 are as follows:

EXPENSES:	Clean Water Fund	Drinking Water Fund	Total
Personnel	\$ 428,297	\$ 308,870	\$ 737,167
Benefits	115,535	89,465	205,000
Contracts	47,243	52,275	99,518
In State Travel	6,741	6,715	13,456
Out of State Travel	3,151	2,402	5,553
Other operating expenses	64,092	64,831	128,923
Capital and non-capital equipment	23,744	-	23,744
Indirect cost	21,250	21,250	42,500
Training and education	-	2,289	2,289
Other operating expenses	81,600	-	81,600
Subtotal	791,653	548,097	1,339,750
Set aside to ADEQ	-	1,108,923	1,108,923
	<u>\$ 791,653</u>	<u>\$ 1,657,020</u>	<u>\$ 2,448,673</u>

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

NOTE 9 AMORTIZATION OF BOND COSTS AND BOND PREMIUMS

WIFA has incurred costs for issuance of bonds, which were not passed on to the borrowers. Such costs are being amortized over the life of the bonds on the straight-line basis. Amortization has been offset against interest expense. Annual amortization for the following bonds is \$125,972 and \$47,287 for Clean Water Revolving and Drinking Water Revolving Funds, respectively. The details follow:

	<u>July 1, 2004</u>	<u>Amortization</u>	<u>June 30, 2005</u>
Clean Water Fund:			
1996A Bonds	\$ 87,555	\$ 7,504	\$ 80,051
1997 Bonds	27,779	5,556	22,223
1998 Bonds	10,228	2,557	7,671
1999 Bonds	534,177	40,571	493,606
2001 Bonds	135,224	19,318	115,906
2004 Bonds	1,059,803	50,466	1,009,337
Drinking Water Fund:			
1998 Bonds	5,044	1,261	3,783
2001 Bonds	123,478	17,639	105,839
2004 Bonds	<u>596,139</u>	<u>28,387</u>	<u>567,752</u>
	<u>\$ 2,579,427</u>	<u>\$ 173,259</u>	<u>\$ 2,406,168</u>

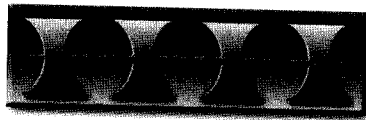
Bond premiums are being amortized over the life of the bonds. Annual amortization for the following bonds is \$1,059,134 and \$621,998 for Clean Water Revolving and Drinking Water Revolving Funds, respectively. The details follow:

	<u>July 1, 2004</u>	<u>Amortization</u>	<u>June 30, 2005</u>
Clean Water Fund:			
1998 Bonds	\$ 32,442	\$ 8,111	\$ 24,331
1999 Bonds	146,980	11,163	135,817
2001 Bonds	821,950	117,421	704,529
2004 Bonds	18,090,647	922,439	17,168,208
Drinking Water Fund:			
1998 Bonds	10,120	2,530	7,590
2001 Bonds	750,554	107,222	643,332
2004 Bonds	<u>10,034,528</u>	<u>512,246</u>	<u>9,522,282</u>
	<u>\$29,887,221</u>	<u>\$1,681,132</u>	<u>\$28,206,089</u>

WATER INFRASTRUCTURE FINANCE AUTHORITY OF ARIZONA
PHOENIX, ARIZONA

COMPLIANCE REPORT

Year Ended June 30, 2005



HENRY & HORNE, LLP
Advisors to Business

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL
REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Board of Directors
Water Infrastructure Finance Authority of Arizona
Phoenix, Arizona

We have audited the financial statements of the Water Infrastructure Finance Authority of Arizona as of and for the year ended June 30, 2005, and have issued our report thereon dated October 4, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Water Infrastructure Finance Authority of Arizona's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Water Infrastructure Finance Authority of Arizona's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have

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CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors
Water Infrastructure Finance Authority of Arizona
Phoenix, Arizona

reported to management of Water Infrastructure Finance Authority of Arizona, in a separate letter dated October 4, 2005.

This report is intended solely for the information of the audit committee, management and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Harry Hertz, LLP

October 4, 2005